2021 DRAFT RESPONSE ON THE 2021 DRAFT TAX BILLS

Presentation to the Standing Committee on Finance (SCoF)

PRESENTED BY:

National Treasury & SARS

Date: 10 November 2021

national treasury

Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

2030 NDP

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CONSULTATION PROCESS

- The 2021 Draft Rates and Monetary Amounts and Amendment of Revenue Laws Bill (Draft Rates Bill) was first published on the same day as the Budget: 24 February 2021.
- The 2021 Draft Rates Bill gives effect to changes in rates and monetary thresholds to the personal income tax tables and increases of the excise duties on alcohol and tobacco.
- The 2021 Draft Rates Bill was published again for the second time for public comment on 28 July 2021, together with the 2021 Draft Taxation Laws Amendment Bill (Draft TLAB) and the 2021 Draft Tax Administration Laws Amendment Bill (Draft TALAB).
- The 2021 Draft TLAB and 2021 Draft TALAB contain the remainder of the tax announcements made in Chapter 4 and Annexure C of the 2021 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 contents.
- This year, a separate Second Batch of the 2021 Draft TLAB and 2021 Draft TALAB was published on 12 August 2021, which contains emergency tax measures in response to the continuing COVID-19 pandemic and recent unrest in the country. These measures are over and above the tax proposals made in the 2021 Budget on 24 February 2021.
- The closing date for public comments on all the 2021 Draft Tax Bills was 28 August 2021.

CONSULTATION PROCESS

- National Treasury and SARS received written comments from 76 contributors on the 2021 Draft Tax Bills by deadline of 28 August 2021.
- National Treasury and SARS briefed the SCoF on the 2021 Draft Tax Bills on 17 August 2021.
- Oral presentations by taxpayers and tax advisors on the 2021 Draft Tax Bills were made at hearings by the SCoF on 31 August 2021.
- Workshops with stakeholders to discuss their comments on the 2021 Draft Tax Bills were held on 7, 8 & 9 September 2021.
- On 10 November 2021, National Treasury and SARS present to the SCoF a draft response document containing a summary of draft responses to public comments received on the 2021 Tax Bills.
- The changes relating to emergency tax measures contained in the Second Batch of the 2021 Draft TLAB and 2021 Draft TALAB are incorporated into the Draft TLAB and Draft TALAB. As a result, the Second Batch of the 2021 Draft TLAB and 2021 Draft TALAB, falls away.

KEY ISSUES RAISED DURING CONSULTATION PROCESS

The key issues raised during public consultation process and during SCoF public hearings are the following:

2021 Draft Rates Bill

- Increase on excise duty on tobacco

2021 Draft TLAB

➢ **Employment, Individuals and Savings**

- Applying tax on withdrawals of retirement interest when an individual ceases to be a tax resident
- Curbing abuse of Employment Tax Incentive
- Strengthening anti -avoidance rules in respect of loan between trusts

➢ **Business Tax (General)**

- Strengthening the rules dealing with limitation of interest deductions in respect of debts owed to certain persons not subject to tax
- Restricting the set-off of the balance of assessed losses in determining taxable income
- Clarifying rehypothecation of collateral within collateral arrangement provisions
- Clarifying the definition of “Contributed Tax Capital”
- Refining the interaction between anti-value shifting rules and cooperate reorganisation rules

KEY ISSUES RAISED DURING CONSULTATION PROCESS

2021 Draft TLAB

➢**International Tax**

- Clarifying the controlled foreign company anti-diversionary rules

➢**Value Added Tax**

- VAT treatment of temporary letting of residential immovable property

➢**Carbon Tax Act**

- Clarifying renewable energy premium beneficiaries
- Clarifying the definition and scope of carbon sequestration-Limitation on biological sequestration to forest plantations
- Aligning schedule 2 emissions activities and thresholds with the greenhouse gas emission reporting regulations of the DFFE

KEY ISSUES RAISED DURING CONSULTATION PROCESS

2021 Draft TALAB

➢ **Income Tax Act**

- Information required in receipts issued for tax deductible donations
- Administrative non-compliance penalties for non-submission of six-monthly employees' tax (EMP501) returns
- Removal of double penalty

➢ **Customs and Excise Act**

- Interpretation of expression "Trade and Industry" where it occurs in certain provisions of the Act
- Deletion of reference to accreditation for purposes of changes in SARS' accreditation system
- Increasing the minimum thresholds for underpayments of duty by taxpayers and payment of refunds by SARS to ease administrative burden

➢ **Tax Administration Act**

- Extension of period within which taxpayer can request revision of an assessment based on an estimate
- Extension of prescription in certain instances

➢ **Disaster Management Tax Relief Administration Act**

- Expansion of deferral of payment of employees' tax liabilities for tax compliant small to medium sized businesses

2021 Draft Rates Bill: Increase in excise duties on alcohol & tobacco

General increase in the excise duty on alcohol and tobacco by 8 per cent (Main reference: Schedule No 1 to the Customs and Excise Act, 1964: clause 5 of the Draft Rates Bill)

***Comments*:** The proposal to increase the excise rate by 8 per cent with the current status of a struggling economy and high unemployment rate of 32.6 per cent is inconceivable. The excise increase is unsustainable and detrimental to the continued survival of the already distressed legal cigarette industry in South Africa.

> ***Response*: Noted**. Excise taxes on tobacco products are intended to reduce consumption and improve public health whilst generating revenue for Government. As stated in the 2021 Budget review, the World Health Organisation recommend an excise incidence of at least 70 per cent to effectively reduce consumption. An 8 per cent increase will shift the excise duty incidence to around 45 per cent.

Comments: The excise hike has placed the excise incidence on the cigarette's Most Popular Price Category (MPPC) at 45 per cent compared to a targeted incidence of 40 per cent as per the National Treasury's excise policy. The total tax incidence on the MPPC now sits at a significant 58 per cent against the background of falling consumer affordability. The excise increase is non-compliant to the extent to which it exceeds Government's own excise policy on tobacco products, being the higher of 40 per cent excise incidence on the MPPC or projected consumer price inflation.

> ***Response: Noted***. Though 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 seeks to ensure that tobacco products do not become affordable over time as this will increase consumption of tobacco products, which goes against public health policy objectives. The targeted incidence of 40 per cent is a policy guideline and need not be followed by Government every year. Given that the incidence has remained above the guideline in recent years, the 2021 Budget Review announced a review on the excise policy framework for tobacco.

General increase in the excise duty on alcohol and tobacco by 8 per cent (Main reference: Schedule No 1 to the Customs and Excise Act, 1964: clause 5 of the Draft Rates Bill)

Comments: National Treasury uses Peter Stuyvesant as the anchor brand in the calculation of the MPPC. However, according to an Ipsos Market Analysis, the MPPC now sits at the low value for money segment, with the anchor brand retailing for R 22.70 (Revised MPPC). Based on the proposed excise rate, excise alone will constitute 85 per cent of the MPPC against an excise policy of 40 per cent of the MPPC. The total tax incidence on the Revised MPPC is 99 per cent – and makes South Africa by far the leading country in the world in terms of total tax incidence on cigarettes. This position is clearly unsustainable and unreasonable. National Treasury should therefore determine the appropriate tax increases based on this Revised MPPC.

> ***Response: Not Accepted***. A revision of the MPPC to the proposed R22.70 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, as announced in the 2021 Budget Review, the excise policy framework for tobacco products is currently under review and some of these issues will be considered; inputs from all stakeholders will also be considered.

Comments: Products with low alcohol by volume (ABV) like beer, should not be viewed through the same lens as other alcoholic products with higher ABV, and the proposed tax rate should not be increased by the same relative percentage as that of other alcoholic products. It is common practice to regulate alcoholic beverages based on beverage type and strength. Many OECD countries tax spirits higher than beer, in terms of excise per litre of pure alcohol. In addition, many use progressive excise taxation within beer, encouraging production and consumption of even lower alcohol strength products. In relation to the harmful nature of alcoholic products, but differentiation with respect to beer, the position by Government expressed by the Minister of Finance in the 2021 Budget Speech that the increase in excise duty of 8 per cent on alcoholic products as a result of the harm associated with these products should not be uniformly adopted in relation to the beer industry. It is therefore advocated that a revised increase at inflation or below should be applied.

General increase in the excise duty on alcohol and tobacco by 8 per cent (Main reference: Schedule No 1 to the Customs and Excise Act, 1964: clause 5 of the Draft Rates Bill)

Response: Noted. Beer is taxed based on alcohol content and the excise duty rate is lower than for spirits (i.e. R115.08 vs. R230.18 per litre of absolute alcohol). Also, this rate structure ensures that beverages with lower alcohol content already have a relatively low tax burden compared to those with higher alcohol content within each category. The suggestion of having a progressive excise duty structure within the beer category has to be taken in the context of administration costs related to having multi-tier tax structures. Before 1998, malt beer used to have an excise duty structure with eight duty bands which were consolidated and simplified.

With regards to having differentiated percentage excise rate increases, it should be noted that everything is considered in the context of the overall fiscal and policy frameworks. It is not always the case that excise rates will increase by the same rate, except in the past 3 financial years. However, as announced in the 2021 Budget Review, the excise policy framework for alcoholic products is currently under review, and inputs from all stakeholders will be considered once the review has been concluded.

Excise duty on Heated Tobacco Products (HTPs)

Comments: The current excise duty on heated tobacco products (HTPs), being 25 per cent less than that of cigarettes, is significantly below the excise tax differential in most of the other countries where these products are now available and where switching from cigarettes, as the most harmful way of consuming nicotine, is being partly driven through excise tax policy. The excise tax for HTPs in the European Union (EU) is on average 72 per cent less than the excise tax on cigarettes. A low excise tax differential, as is the case in South Africa, could be viewed as de facto support for cigarettes and other combusted tobacco products.

> ***Response: Not Accepted***. Excise taxes on all tobacco products are intended to reduce consumption and improve public health. In line with the World Health Organisation’s Framework Convention on Tobacco Control’s guiding principles, specifically, the one contained in Article 4.2(b), we also intend to discourage initiation because Government recognises that all forms of tobacco use are harmful, including the use of HTPs. The concessionary rate given to HTPs should not be interpreted as de facto support for either cigarettes or HTPs, but as an introductory rate that is subject to review. A cautionary approach is necessary because as argued by the World Health Organisation (2020:8):
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> “…there is insufficient evidence to conclude that HTPs are less harmful than conventional cigarettes. In fact, there are concerns that while they may expose users to lower levels of some toxicants than conventional cigarettes, they also expose users to higher levels of other toxicants. It is not clear how this toxicological profile translates into short- and long-term health effects”.

Comments: Considering the vastly different characteristics and risk profiles of non-combusted tobacco and nicotine products compared to combusted tobacco products, combusted tobacco products should be taxed significantly higher than non-combusted tobacco and nicotine products as this would accelerate a complete switch from cigarettes and other combusted tobacco products. It is recommended that the excise tax on non-combusted tobacco and nicotine products should be below the lowest excise tax level applied to any combusted tobacco product.

> ***Response: Not Accepted.*** Even though the new generation products such as HTPs and ENDS are different from the traditional tobacco products, a cautionary approach should be taken with regards to significant rate differentiation as indicated in the response above. However, this is an interesting policy development area that will be monitored over the coming years as more evidence on the short- and long-term effects develops.

Illicit trade of alcohol and tobacco products

Comments: It's important for Government to use excise policy to suppress the growth of the illicit market, by closing the gap between duty not paid (DNP) and duty paid (DP) prices, through gradual excise increases typically in line with inflation. This allows the recapture of illicit volumes into the legal market and the meeting of public health objectives (which include the reduction of consumption from both the legal and illegal market).

> ***Response: Noted.*** The problem of illicit trade cannot be sorted out through the excise rate adjustments but needs to be effectively addressed through robust compliance and law enforcement mechanisms. SARS has been working hard to rebuild internal capacity and has also, through the Inter-Agency Working Group (IAWG) on Illicit Trade, been implementing compliance and enforcement measures. This is evident from a number of raids, seizures and destruction of illegal cigarettes conducted recently as profiled in the media. Examples from the last 3 months:
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> - https://www.sars.gov.za/media-release/unregistered-tobacco-manufacturing-plant-uncovered/
> - https://www.sars.gov.za/media-release/r10-million-of-illicit-cigarettes-declared-as-tissue-paper/
> - https://www.sars.gov.za/media-release/sars-seizes-illicit-cigarettes-valued-at-r6-million/

Comments: It is only after an effective excise collection system, which evidently collects full excise from all manufactures and importers, has been put in place that the existing excise policy be reviewed. An effective customs and excise administration system for the tobacco industry must include: the immediate enforcement of the SARS Productions Counter Rules by all local manufacturers; production counters which will allow SARS to reconcile local production volume with excise payments and export declarations; end-to-end frequent and comprehensive audits of all manufacturers; stricter border control and enforcement; the ratification of the WHO FCTC Illicit Trade Protocol; and the implementation of an independent track and trace system consistent with the FCTC Illicit Trade Protocol and Guidelines.

Illicit trade of alcohol and tobacco products

Response: Not Accepted. 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. The two processes are not mutually exclusive. SARS is implementing a number of compliance measures, including collaborating with other law enforcement agencies and industry to address issues in the tobacco supply chain. Furthermore, 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.

Comments: Ipsos was commissioned to conduct a representative Retail and Wholesale price research and found that 41 per cent of the cigarettes sold in South Africa are below the minimum collectable tax (i.e. excise and VAT payable) for a pack of cigarettes. Further, 64 per cent were sold below the economically viable retail price of R26.55 for a pack. The economically viable retail price takes into account, the direct costs and the lowest possible margins required to bring a pack of cigarettes into the market. In our view, an effective customs and excise administration system for the tobacco industry must include the implementation and full enforcement of a Minimum Retail Sales Price of R28 for 20 sticks.

Response: Noted. The issue of Minimum Retail Sales Price is a new proposal in terms of the current policy regime. The excise policy framework for tobacco products is currently under review. Inputs from all stakeholders such as this will be considered.

Comments: While the reasons provided for not adhering to policy focuses on the harm associated with the abuse of alcohol, in our view the said increase in alcohol taxes is not the solution, as it has some unintended consequences of increasing the illicit trade in South Africa. A recent Euromonitor Report (2020) confirms that the sale of illicit alcohol products in South Africa now accounts for 22 per cent of the alcohol market by volume, and 12 per cent by value, which equates to R20.5bn. The losses to the fiscus accounts for a staggering R11.3bn which has seen a growth of 20 per cent (CAGR), since the report was last commissioned in 2017.

Response: Noted. Government is aware of the studies conducted regarding the problem of illicit trade in alcoholic products, especially during the various periods of trade restrictions imposed by Regulations issued in terms of the Disaster Management Act, 2002. Illicit trade is a concern for Government, both in terms of undermining public health and harm reduction objectives, and fiscal collections. There are however efforts from both SARS and the law enforcement agencies to address the problem.

2021 Draft TLAB: Employment, Individuals and Savings

Applying tax on withdrawals of retirement interest when an individual ceases to be a tax resident

(Clauses 11 of the Draft TLAB: New section 9HC of the Income Tax Act)

- When an individual ceases to be a South African tax resident before he/she retires and becomes a tax resident of another country, that individual's retirement fund interest may be subject to tax in the other country, due to the application of the tax treaty between South Africa and the other country.
- The provisions of the tax treaty between South Africa and the other country will regard the individual to be a tax resident in that other country, thereby in some instances resulting in South Africa forfeiting its taxing rights , while the taxpayer benefited from tax deductions in respect of contributions to the retirement fund.
- To address this, the following proposed changes were included in the 2021 Draft TLAB:
  - When an individual ceases to be a South African tax resident, the retirement fund interest will form part of the assets that are subject to retirement withdrawal tax. The individual will be deemed to have withdrawn from the fund on the day before he/she ceases to be a South African tax resident
  - When an individual ceases to be a South Africa tax resident but leaves his/her investment in a South African retirement fund and only withdraws from the retirement fund when he/she dies or retires from employment, then the retirement withdrawal tax including associated interest will be deferred until payments are received from the retirement fund or as a result of retirement. When the individual eventually receives payment from the fund, the tax will be calculated based on the prevailing lump sum tables or in the form of annuity. A tax credit will be provided for the deemed retirement withdrawal tax as calculated when the individual ceases to be a South African tax resident.

Applying tax on withdrawals of retirement interest when an individual ceases to be a tax resident

(Clauses 11 of the Draft TLAB: New section 9HC of the Income Tax Act))

- ***Comment***: Bypassing tax treaties with domestic legislation is controversial and could potentially result in double taxation for members of retirement funds. Should the Government still wish to address the concern of erosion of the tax base due to emigration, the relevant DTA's that are of concern to the Government should be renegotiated accordingly. In addition, the proposed insertion of section 9HC will lead to involuntary withdrawals of retirement interests upon emigration. Members will therefore be required to withdraw from their retirement funds in South Africa, even if they did not envisage doing so and rather preferred to retain their retirement savings in South Africa. Consequently, the recent introduction of the 3-year rule still requires clarity from an administrative point of view, and taxpayers are still seeking clarity on its application; adding a new layer of complexity will further complicate the emigration process, resulting in expensive administrative costs to taxpayers.

  ***Response*: Noted**. Although the rationale behind the proposed amendments is understood by the public, numerous concerns that the proposed amendments will result in a case of treaty override are noted by Government. Following the extensive public participatory deliberations with members of the public in Parliament and through public consultation process hosted by National Treasury on the 2021 Draft Tax Bills, the proposed amendments dealing with applying tax on withdrawals of retirement interest when an individual ceases to be a tax resident contained in new section 9HC will be withdrawn from the 2021 Draft TLAB and further amendments will be considered in the next legislative cycle in order to address the complexities that were raised through public comment process.

Curbing abuse in the Employment Tax Incentive

(Clauses 58 & 59 of the Draft TLAB: Definition of "employee" and section 6 of the ETI Act)

- The Employment Tax Incentive (ETI) programme was introduced in January 2014 to provide for employment of young workers and make provision for employers to reduce their pay-as-you-earn (PAYE) tax payments to the South African Revenue Service (SARS) for the first two years in which they employ qualifying employees with a monthly remuneration of less that R6 500, subject to certain limitations.
- It has come to Government's attention that some taxpayers have devised certain schemes to claim the incentive in respect of individuals who do not work for them, but are rather engaged in training programmes using training institutions, with no employment characteristics (therefore failing to meet the definition of 'employee' as defined in section 1(1) of the ETI Act).
- To counter this abuse, the following proposed changes were included in the 2021 Draft TLAB :
  - 'work' must actually be performed in terms of an employment contract and the employee must be documented in the employer's records as envisaged in the record keeping provisions contained in section 31 of the Basic Conditions of Employment Act.
  - In view of the fact that the proposed changes to the legislation are aimed at curbing abusive schemes, it was further proposed that these amendments should apply retrospectively and be deemed to have come into operation on 1 March 2021

Curbing abuse in the employment tax incentive

(Clauses 58 & 59 of the Draft TLAB: Definition of "employee" and section 6 of the Employment Tax Incentive Act)

- ***Comment***: The proposed amendments to section 6 of the ETI Act result in what are actually legitimate ETI claims no longer qualifying for the incentive. As a result, instances where the employer provides on the job training, where the employer and employee have entered into a learnership or apprenticeship programme, or where the employee is on a secondment may no longer qualify for the incentive. Consideration should rather be given to clarifying that the employee should be given a cash payment in lieu of services rendered.

  ***Response*: Accepted**. The incentive is intended to apply to all legitimate arrangements where the employee is not only engaged in the activity of studying, but rather gaining valuable work experience. In the event that some of the employee's duties involve some sort of training or studying, the costs of said training or studying should ideally be borne by the employer. To ensure that the employee's remuneration package is not solely allocated to costs associated with any required training or studying, qualification for the incentive shall further be based on the employee receiving a cash payment in lieu of services rendered. Changes will be made in the 2021 Draft TLAB to reflect this intention.

Curbing abuse in the employment tax incentive

(Clauses 58 & 59 of the Draft TLAB: Definition of "employee" and section 6 of the ETI Act)

- ***Comment***: The proposed amendment's effective date should rather be postponed. Consideration should be given to postponing the effective date from 1 March 2021 to 28 July 2021, which is the date of publication of the draft TLAB for public comment as the amendment in its current form results in legitimate claims made during the 2021/2022 tax year now being unlawful.

  ***Response:* Partially Accepted.** Given the uncertainty around specific issues pertaining to the draft legislation and in the interest of ensuring that claims that would have otherwise been legitimate are not deemed unlawful, changes will be made in the 2021 Draft TLAB to postpone the effective date from 1 March 2021 to 1 March 2022.

- ***Comment***: It is noted that paragraphs (a) to (d) of the definition of employee in the ETI Act are intended to be applied cumulatively, (i.e. all of the five requirements must be met for the person to be an employee). It is however unclear how paragraph (c) is intended to apply in addition to paragraph (a); is paragraph (c) meant to be an alternative to paragraph (a)?

  ***Response*: Accepted**. Paragraph (c) of the definition of employee in the ETI Act is not intended as an alternative to paragraph (a) as the intention is for both paragraphs to apply simultaneously. The uncertainty created is however noted and changes will be made in the 2021 Draft TLAB to clarify this.

Strengthening anti-avoidance rules in respect of loan transfers between trusts

(Clause 5 of the Draft TLAB: Section 7C of the Income Tax Act)

- In 2016, anti-avoidance measures were introduced to curb the tax-free transfer of wealth to trusts using low interest or interest-free loans in order to avoid estate duty and donations tax on the assets subsequent growth in value. In 2017 and in 2020, further changes were made to counter new attempts to undermine these measures.
- Government is concerned about further tax avoidance schemes between trusts, where the founder of one trust holding the original asset is related to one or more beneficiaries of the other trust to which the loan asset is transferred.
- To address this, the following proposed changes were included in the 2021 Draft TLAB
  - The anti-avoidance rules will also apply in respect of any loan, advance or credit that a trust, directly or indirectly provides to another trust in relation to which, its beneficiaries or the founder are connected persons in relation to the founder or beneficiaries of the trust that provided the loan, advance or credit.
  - In view of the fact that the proposed changes are aimed at curbing tax avoidance schemes, it was further proposed that these amendments should apply retrospectively and be deemed to have come into operation on the date of the publication of the 2021 draft TLAB for public comment, i.e., 28 July 2021.

Strengthening anti-avoidance rules in respect of loan transfers between trusts

(Clause 5 of the Draft TLAB: Section 7C of the Income Tax Act)

- ***Comment:*** The proposed amendments aim to ensure that the anti-avoidance measures apply in respect of any loans, advances or credit that a trust, directly or indirectly provides to a trust in relation to which, its beneficiaries or the founder are connected persons in relation to the founder or beneficiaries of the trust that provided the loan, advance or credit. Section 7C was originally introduced to counter schemes whereby a person transfers his or her growth assets to a trust in return for a fixed loan without interest in order to avoid wealth taxes (donations tax or estate duty) on the growth asset. The proposed amendment should be withdrawn and alternative anti-avoidance measures aimed at the specific mischief, namely transactions that result in a tax free disinvestment in a South African company followed by an investment in a company in another jurisdiction, should be considered.

***Response*: Accepted.** Although a risk was identified that through the use of low interest bearing or interest free loans between trusts, taxpayers could achieve tax free disinvestments from South African companies facilitated through loan arrangements. However, it is acknowledged that the aim of section 7C was to specifically curb the use of low interest bearing or interest free loans in order to avoid estate duty and donations tax on the assets subsequent growth in value. As such, the changes proposed in the 2021 Draft TLAB will be withdrawn and a more specific anti-avoidance measure will be considered in the future.

2021 Draft TLAB: Business (General)

Strengthening the rules dealing with limitation of interest deduction in respect of debts owed to certain persons not subject to tax

(Clause 20 of the Draft TLAB: Section 23M of the Income Tax Act)

- In 2013, rules that limit interest deductions in respect of debts owed to persons not subject to tax were introduced in the Act (apply in respect of amounts of interest incurred on or after 1 January 2015).
- Main aim of these rules is to limit excessive interest deductions in respect of debts owed to persons not subject to tax in South Africa, if the debtor and the creditor are in a controlling relationship.
- 26 February 2020 – Government published a discussion document titled "***Reviewing the Tax Treatment of Excessive Debt Financing, Interest Deductions and Other Financial Payments***" to conduct a review of the current rules in comparison to the OECD/G20 BEPS Action 4 recommendations.
- To strengthen the rules in line with the recommendations, the following proposed changes were included in the 2021 Draft TLAB (as part of a corporate tax package):
  - Expanding the meaning of the term "*interest*" for purposes of these rules
  - Moving to a fixed ratio (30% of earnings) restriction rather than one based on a formula
  - Reducing opportunities to avoid the rules with back-to-back loans
  - Amending the definition of "*adjusted taxable income*" as it applies to REITs
  - Interaction between the level of tax on interest and the current rules

Strengthening the rules dealing with limitation of interest deduction in respect of debts owed to certain persons not subject to tax

(Clause 20 of the Draft TLAB: Section 23M of the Income Tax Act)

- *Comment:* Companies' earnings have been severely affected by COVID-19. If this proposal is introduced in the years where the impact of the COVID-19 pandemic is felt, interest deductibility will be further impacted by the significantly lower tax EBITDA in the current and post COVID-19 pandemic years.
    - *Response:* <u>Accepted</u>. This measure was first proposed before Covid-19 reached South Africa. The current rules are an important tool to mitigate the use of excessive debt and interest payments that reduce taxable profits in South Africa. Government maintains the view that these rules need to be strengthened to protect the corporate tax base, but understands that many businesses may have had to rely on more debt to withstand the pandemic and its associated lockdowns. This coupled with lower earnings provides the rationale for postponing this proposal to provide space for recovery. The proposal will remain in the 2021 Draft TLAB. However, the proposals will come into operation on the date on which the rate of tax in respect of the taxable income of a company is first reduced after announcement by the Minister of Finance in the Annual National Budget, and will apply in respect of years of assessment commencing on or after that date.

Strengthening the rules dealing with limitation of interest deduction in respect of debts owed to certain persons not subject to tax

(Clause 20 of the Draft TLAB: Section 23M of the Income Tax Act)

- *Comment:* The proposed 30 per cent ratio is generally applicable to developed countries, not developing countries like South Africa. It will make South Africa unattractive as an investment destination.
  - *Response:* Not Accepted*.* South Africa is not the only developing country that has implemented these rules as recommended by the OECD/G20 BEPS Project. Countries like Botswana and India have also implemented a fixed ratio rule at 30 per cent. As stated in the Explanatory Memorandum, Government's analysis at the outset of these rules suggested that 40 per cent was too high even though interest rates at that time were higher than currently.
- *Comment:* The definition of "controlling relationship" does not cover a scenario where a company is under the joint control of persons and creates a loophole as a result. For example, if in a large multinational setting – a loan is advanced from a treasury company that is a fellow-subsidiary of the South African borrower, the interest expense will not be subject to the rules.
  - *Response:* Accepted. Changes will be made to the definition of "controlling relationship" in the 2021 Draft TLAB to cover companies that are directly or indirectly under a common controlling relationship.

Strengthening the rules dealing with limitation of interest deduction in respect of debts owed to certain persons not subject to tax

(Clause 20 of the Draft TLAB: Section 23M of the Income Tax Act)

- *Comment:* The proposal should apply only to interest that is not subject to tax – it is inappropriate to adjust for rate considerations, particularly when the tax base is different. The proposal will result in interest that is subject to interest withholding tax at 15 per cent being subjected to the partial application of section 23M. The proposal should be with reference 15, not 28 per cent.
  - *Response:* Partially Accepted. As explained in the Explanatory Memorandum, the current rules have a different application depending which country the affected interest payments are flowing to, due to reduced interest withholding tax rates. Government is of the view that it is fairer to equalise the treatment depending on how much tax is actually paid. To recognise that the tax base for corporate income tax and withholding taxes is different, changes will be made in the 2021 Draft TLAB to replace the reference to the current corporate income tax rate of 28 per cent with the standard dividends tax rate of 15 per cent.

Restricting the set-off of the balance of assessed losses in determining taxable income

(Clause 19 of the Draft TLAB: Section 20 of the Income Tax Act)

- In determining taxable income, taxpayers can set off their balance of assessed losses carried forward from the preceding tax year against their income. An unutilised balance of assessed losses may be carried forward to future years of assessment to be set off against future income (provided that the non-individual taxpayer’s trade continues without interruption).
- Accordingly, taxpayers will only be liable for income tax once they have earned a taxable profit and their assessed loss balance is depleted. The purpose of providing for the deductibility of assessed losses for corporate taxpayers is to smooth the tax burden for companies whose primary business is cyclical in nature and not in line with a standard tax year, and for start-up companies that are not profitable in the early years of trading.
- Over the past few years, there has been an international trend to restrict the use of assessed losses and reduce the corporate income tax rate. To improve the country’s competitiveness, reduce the appeal of base erosion and profit shifting, encourage investment and promote economic growth, the Minister of Finance announced (in the 2020 Budget Review) Government’s intention to restructure the corporate income tax system over the medium term by broadening the base and reducing the corporate income tax rate in a revenue neutral manner.
- In the 2021 Draft TLAB (as part of the corporate tax package), Government proposed broadening the corporate income tax base by restricting the offset of the balance of assessed losses carried forward to 80 per cent of taxable income. The effect of the proposed restriction is that only companies that would be in a positive taxable income position before setting off the balance of assessed losses would be affected. While the overall tax liability will not change, a portion of the tax liability will be brought forward.

Restricting the set-off of the balance of assessed losses in determining taxable income

(Clause 19 of the Draft TLAB: Section 20 of the Income Tax Act)

- *Comment:* Most commentators understand and appreciate the overall objective of broadening the corporate tax base and lowering the tax rate. However, one of the biggest concerns raised was timing – that the proposal is too harsh given the continuing Covid-19 pandemic and recent unrest in the country. Many businesses (in different sectors, large and small) have suffered losses as a result of the pandemic and associated lockdowns. Having to use cash to pay tax on 20 per cent of taxable income rather than using cash flows to recover and reduce debt will place an additional burden on companies that are trying to recover from these adverse events. Many countries have temporarily relaxed their tax loss regimes as part of the relief measures to support businesses in these times.
  - *Response*: Accepted. This measure was first proposed before Covid-19 reached South Africa. Government holds the view that a broad tax base with as few distortions as possible, combined with a lower rate, will be more efficient – an important tax policy design principle. It is also acknowledged that businesses have faced difficult economic circumstances in the past 19 months. Some businesses are in survival mode and providing the space for recovery is important. For this reason, the proposal will remain in the 2021 Draft TLAB. However, the proposals will come into operation on the date on which the rate of tax in respect of the taxable income of a company is first reduced after announcement by the Minister of Finance in the Annual National Budget, and will apply in respect of years of assessment commencing on or after that date.

Restricting the set-off of the balance of assessed losses in determining taxable income

(Clause 19 of the Draft TLAB: Section 20 of the Income Tax Act)

- *Comment:* Commentators raised a number of concerns with respect to the impact on different types of businesses (e.g. cyclical, start-ups, smaller businesses) and specific sectors.
  - *Response:* Partially Accepted. As a general stance, Government is not in favour of providing carve-outs because they provide special treatment to some taxpayers and can lead to complexity. This has the potential to create vested interests for those that benefit – making it difficult to adapt the original policy choice if it becomes apparent that it is not ideally designed or no longer fit for purpose. It also often means that Government is continually exposed to lobbying from those who do not benefit because they also consider themselves eligible for special treatment.
  - Although the proposed quantum restriction is relatively generous at 80 per cent and one of the least punitive given that companies will not forfeit any losses and the balance of assessed losses will continue to be carried forward indefinitely, Government recognises that not all businesses are equally equipped with cash on hand once taxable income turns positive for the first time after a sustained period of accumulated losses.
  - To cater for all sectors and recognise that not all companies have sufficient cash flow to face an additional tax burden in the first year they become profitable, Government proposes that changes be made in the 2021 Draft TLAB to introduce a *de minimis* threshold beyond which the proposal takes effect. The aim is to provide breathing room for a variety of companies that may experience cash flow challenges at different times. To the extent that the balance of assessed loss exceeds 80 per cent of current-year taxable income, companies will be able to set off the higher of R1 million or 80 per cent of taxable income when calculating their tax liability.
  - While other countries have higher thresholds, they also have more punitive restrictions in place. This threshold means that the corporate income tax package will not move too far away from its aim of revenue neutrality given the currently constrained fiscal space.

Restricting the set-off of the balance of assessed losses in determining taxable income

(Clause 19 of the Draft TLAB: Section 20 of the Income Tax Act)

- *Comment:* Commentators from the agricultural sector raised concerns that this measure would have a negative impact on them, given the cyclical nature of their business and the negative impact of Covid-19 and its associated lockdowns.
  - *Response*: <u>Partially Accepted.</u> In line with Government's general stance on carve-outs, no special treatment will be provided for the agricultural sector, however the *de minimis* of R1 million will help smaller incorporated farmers who experience cyclical profitability. Taxpayers sent written comments prior to the Parliamentary hearings (held on 31 August 2021) and taxpayer workshops (held on 7 September 2021). In the workshops, slides were presented to explain the rationale behind the corporate tax package and the mechanics of this proposal. A representative from the agricultural sector recognised that there was initially a partial misinterpretation and welcomed the fact that losses can continue to be carried forward, i.e. they will not be forfeited.

Restricting the set-off of the balance of assessed losses in determining taxable income

(Clause 19 of the Draft TLAB: Section 20 of the Income Tax Act)

- *Comment:* The proposal, combined with no extension of the tax benefits for REITs to unlisted property companies, means that most (if not all) unlisted property funds will pay tax. This reinforces the uneven playing field between listed REITs and unlisted property companies.
  - *Response*: <u>Partially Accepted</u>. Government accepts that this uneven playing field is a challenge for the unlisted companies. However, the proposal itself is not the root cause of this challenge, so providing a carve-out is, in Government's view, not deemed appropriate. The underlying challenge is a lack of regulation of unlisted property companies.

- *Comment:* There is a need for the individual policyholder fund (IPF) to be carved out of the proposed amendment as the policyholders of the IPF consist solely of individuals who are not intended to fall within the scope of this amendment. IPFs would not get relief from a reduced company tax rate as would any other company.
  - *Response*: <u>Not accepted</u>. Government acknowledges that this measure would affect individuals with investments in IPFs. However, the tax rate of 30 per cent applied to these funds is already lower than the majority of the individual policyholders' marginal tax rates. While Government would prefer actual marginal tax rates to apply on an individual basis, it is recognised that this is not a solution for the challenge and commits to reinvestigate the tax rate applied in respect of the IPF. No special treatment will be applied to the IPF in respect of this proposal.

Clarifying rehypothecation of collateral within collateral lending arrangements

(Clause 56 of the Draft TLAB: Section 1 of the Securities Transfer Tax Act)

- The Act contains tax relief rules that allow for the tax neutral transfer of collateral (listed shares or local and foreign government bonds) between the parties to a collateral arrangement, provided that certain requirements are met.
- At issue is the rehypothecation of collateral, where the bank, broker dealer or collateral taker (transferee) intends to use that collateral received through a tax-neutral collateral arrangement for trading or as security for its own borrowing.
- The use of collateral for purposes other than subsequent collateral arrangements is against the policy rationale for the introduction of these provisions and could result in the avoidance of securities transfer tax or capital gains tax.
- To address this, the following proposed changes were included in the 2021 Draft TLAB:
  - The shares or bonds transferred as collateral in terms of a collateral arrangement may subsequently only be used for collateral and not be used for trading or in other financial transactions.
  - The transferee enters into a contractual arrangement and agrees that the listed share or listed bond transferred in terms of the collateral arrangement will either be held by that transferee for the duration of the arrangement or be used for purposes of providing security in respect of an amount owed by that transferee
  - In view of the fact that the proposed amendments are aimed at curbing abuse, it was proposed that these amendments should apply retrospectively and come into operation on the date of the publication of the 2021 draft TLAB for public comment. i.e. 28 July 2021.

Clarifying rehypothecation of collateral within collateral lending arrangements

(Clause 56 of the Draft TLAB: Section 1 of the Securities Transfer Tax Act)

- ***Comment:*** There is no need to introduce the proposed legislative limitation on the rehypothecation of collateral (or a need for any amendment) as the existing legislation is perfectly adequate in ensuring that any re-use of collateral outside of a further collateral arrangement or a lending arrangement, would fall within the tax net The Act contains tax relief rules that allow for the tax neutral transfer of collateral (listed shares or local and foreign government bonds) between the parties to a collateral arrangement, provided that certain requirements are met.

  Response: **Not Accepted.** The tax-free measures in support of collateral arrangements are an incentive and deviate from general tax principles which necessitated extensive engagement with financial sector participants in the run-up to the 2015 introduction of 'collateral arrangements' within the STT Act and the Income Tax Act. It was widely accepted then that financial sector participants understood the assumptions of the tax-free flow of collateral and what the inferred tax implications would be if that transactional flow of collateral fell outside of the intended legislated structure. However, several financial sector participants have requested clarity on the policy intent and scope of rehypothecation under collateral arrangements.

- ***Comment:*** The retrospectivity of the proposed legislation, which is the date of publication of the 2021 Draft TLAB for public comment has resulted in significant practical concerns. The proposed amendment not only requires the collateral taker to not re-use the collateral for non-collateral purposes, but also requires the collateral taker to contractually agree to this. Thus, even if a collateral taker were not to re-use collateral for non-collateral purposes, without amending the industry standard agreement governing collateral, that any collateral placed on or after 28 July 2021 would fall outside the proposed contractual ambit of the tax-free collateral arrangements' dispensation. Agreements governing collateral transactions are based on widely accepted international standards/templates and amending these agreements, barring the required sufficient lead time nationally, puts South Africa at a disadvantage as international counter parties might be unwilling to agree to any contractual inclusion of a restriction on the re-use of the collateral.

  ***Response:* Accepted**. Changes will be made in the 2021 Draft TLAB to remove the contractual requirement and that the effective date be postponed from the date of publication of the 2021 Draft TLAB for public comment to 1 January 2022.

Clarifying rehypothecation of collateral within collateral lending arrangements

(Clause 56 of the Draft TLAB: Section 1 of the Securities Transfer Tax Act)

- ***Comment:*** It is recognised and supported that Government should have the ability to clarify policy intent or to identify and sanction the improper use of collateral which possibly results in the avoidance of tax. However, the current proposed wording is very wide in its impact and also threatens to have a material negative impact on both regulatory conduct and then the liquidity, stability and attractiveness of the South African capital markets, through the:
  - inability of banks and pensions funds to meet regulatory obligations, the very underlying purpose of introducing the 2015 collateral arrangement dispensation, including:
  - banks being unable to re-use collateral for HQLA purposes;
  - inability of pension funds to now meet Regulation 28 requirements;
  - re-use of collateral for security optimisation within a bank or pension fund;
  - the sale and transfer of securities (generally Government bonds) by the banks to the SARB, which securities include outright non-cash collateral taken by banks; and
  - the Large Exposures Framework (LEX)

Response: **Partially Accepted.** Changes will be made in the 2021 Draft TLAB to accommodate the following regulated transactions and current market and regulatory developments:

- A repurchase agreement entered into with the South African Reserve Banks in terms of section 10(1)(j) of the South African Reserve Bank Act;
- Complying with Regulation 28 of the Pension Funds Act
- Securing overnight cash placement in order to comply with the Basel III Supervisory Framework for measuring and controlling large exposures

Clarifying the definition of "contributed tax capital"

(Clause 4(1)(c) of the Draft TLAB: Section 1 of the Income Tax Act)

- The concept of contributed tax capital (CTC) was introduced in the Act in 2008. The CTC of any company is a notional and ring-fenced amount derived from contributions made to a company by holders of a class of shares as consideration for the issue of that class of shares by that company. It is reduced by any capital amount that is subsequently transferred back by the company to one or more shareholders of that class of shares (commonly known as a capital distribution) utilising the notional tax amount so received. No shareholder within a particular class of shares may receive CTC in excess of an amount per share that is derived by dividing the total CTC by the number of shares in that class immediately before the capital distribution.
- It has come to Government's attention that some companies are exploiting the current provisions of CTC by allocating CTC on the basis of an alleged "share premium" contributed by a particular shareholder but not to all shareholders holding shares in the same class of shares.
- To address this, proposed changes were made to the definition of CTC in the 2021 Draft TLAB to clarify the principle that shareholders within the same class of shares should share equally in the allocation of CTC as a result of a distribution.

Clarifying the definition of "contributed tax capital"

(Clause 4(1)(c) of the Draft TLAB: Section 1 of the Income Tax Act)

- ***Comment:*** The proposed amendment seeks to clarify the principle that shareholders within the same class of shares should equally, in relation to their shareholding, share in the allocation of CTC as a result of a distribution. However, the proposed wording potentially has a much wider impact than intended, especially on the corporate actions of elective share buy-backs (per section 48 of Companies Act) and redeemable preference shares. Elective share buy-backs generally only apply to specific shareholders in a particular class and as such, and by the very nature of the proposed amendment, any elective share buy-back action will be automatically excluded from the utilisation of CTC and classified as a dividend as not all shareholders within that class, will benefit from that repurchase (distribution) through CTC. On a similar basis, redeemable preference shares, whilst in the same class, redemptions may be staggered over a number of tranches, maturity dates or where different holders are redeemed at different times. As such it is recommend that both elective share buy-backs and redeemable preference shares are excluded from the ambit of the proposed proviso in the TLAB 2021. Companies effecting a specific share buy-back should be permitted to return CTC proportionally to the percentage of shares which are the subject of the repurchase.

  ***Response:* Partially Accepted.** Changes will be made in the 2021 Draft TLAB to exclude a general repurchase of listed shares (share buy-backs) by companies listed on the JSE or other South African exchanges.

Clarifying the definition of "contributed tax capital"

(Clause 4(1)(c) of the Draft TLAB: Section 1 of the Income Tax Act)

- ***Comment:*** The current proviso to the definition of CTC states that "the amount transferred by a company…must not exceed an amount that bears to the total amount of contributed tax capital to that class of shares immediately before the transfer the same ratio as the number of shares of that class held by that person bears to the total number of shares of that class". This wording creates unintended tax consequences for a shareholder that makes a large capital contribution to a company, but by virtue of the wording of this proviso, may only be able to receive a portion of a distribution by that company as CTC, proportionate to its diluted shareholding and not its shareholding in the company because of its actual capital contribution.

  ***Response:* Not Accepted.** The comment falls outside the context of the proposed amendment in 2021 Draft TLAB. However, it is important to note that the current wording included in the 2021 Draft TLAB is aimed at striking a balance between the extensive administrative burden required to match every CTC contribution and then the ease of applying any form of ratio.

- ***Comment:*** The proposed further proviso will be deemed to come into effect on the date of publication of the Draft TLAB for public comments. Given that there are potentially a number of transactions that are currently in progress which would be impacted by the additional proviso, it potentially could result in adverse tax consequences for transactions that are being implemented from the date of the publication of the Draft TLAB for public comments and its ultimate promulgation which in turn also creates uncertainty in the market.

  Response: Accepted. Changes will be made in the 2021 Draft TLAB to change the retrospective effective date of the proposed amendment from the date of publication of the 2021 Draft TLAB for public comment , i.e. 28 July 2021 to 1 January 2022.

Refining the interaction between anti-value shifting rules and corporate reorganization rules

(Clause 25 of the Draft TLAB: Section 40CA of the Income Tax Act)

- The Act contains anti-value shifting rules in sections 24BA and 40CA that curb the use of structures that shift value between taxpayers free of tax.
- On the other hand, the corporate reorganisation rules allow for the tax neutral transfer of assets between companies.
- The interaction between the anti-value shifting rules in sections 24BA and 40CA and the corporate reorganisation rules gives rise to anomalous results as the capital gain triggered under the anti-value shifting rules is only added to the base cost of an asset acquired in exchange for the issue of shares by a company in terms of section 40CA, which is outside of the corporate reorganisation rules.
- To rectify this anomaly, the following changes were included in the 2021 Draft TLAB:
  - To provide for additional base cost equal to any deemed capital gain resulting from the application of the anti-value shifting rules in section 24BA for corporate reorganisation rules
  - However, such additional base cost is not required until a taxpayer subsequently disposes of an asset by way of a transaction that is not tax deferred in terms of the corporate reorganisation rules. As a result, it is proposed that a company will be deemed to have incurred expenditure equal to the triggered deemed capital gain immediately before a subsequent disposal of an asset, previously acquired in terms of the above-mentioned reorganisation provisions, in a transaction that falls outside corporate reorganisation rules.

Refining the interaction between anti-value shifting rules and corporate reorganization rules

(Clause 25 of the Draft TLAB: Section 40CA of the Income Tax Act)

- ***Comment***: The changes proposed are welcomed. However, it is noted that the proposal for the additional base cost only to be deemed to arise immediately prior to a subsequent disposal introduces an additional, and unnecessary, level of complexity and administration. In particular, there are concerns around the complexity this will lead to when making determination for deferred tax as it becomes debatable what the base cost an asset whose transfer that was subject to the anti-value shifting rules and has not yet been disposed of outside of the corporate reorganisation rules is. As such, it is requested that the additional base cost uplift should be granted upfront immediately after an asset-for-share transaction that is subject to the anti-value shifting rules.

***Response*: Accepted.** Changes will be made in the 2021 Draft TLAB to ensure that the additional base cost uplift in this regard, is granted immediately after an asset-for-share transaction that is subject to the anti-value shifting rules. As a consequential amendment, an additional legislative change will be made to section 41(2) of the Act to ensure that the re-organisation rules are made subject to this immediate base cost uplift.

2021 Draft TLAB: International Tax

Clarifying the controlled foreign company anti-diversionary rules

(Clause 10 of the Draft TLAB: Section 9D(9A) of the Income Tax Act)

- The Act contains Controlled Foreign Company (CFC) anti-avoidance provisions in section 9D aimed at taxing South African residents on the net income of a CFC. In order to strike a balance between protecting the South African tax base and the need for South African multinational entities to be competitive, the CFC rules contain various exemptions of certain types of business income, for example, the foreign business establishment exemption.
- This exemption makes provision for CFC income to be exempt if that income is attributable to a foreign business establishment as defined in section 9D of the Act. In order to limit tax avoidance, the foreign business establishment exemption does not apply if the CFC foreign business establishment income is regarded as diversionary foreign business income in terms of the CFC anti-diversionary rules.
- It has come to Government's attention that certain taxpayers are circumventing the rule by merely entering into a contract of purchase in the country of the CFC that implies that the purchase of goods took place in the country of residence of the CFC when the goods are never physically present in that country.
- It was proposed in the 2021 Draft TLAB that the diversionary rules focusing on the purchase of goods by CFCs be amended to provide clarity on the tax policy intent that when a CFC purchases goods, they should be delivered in the country of residence of that CFC.

Clarifying the controlled foreign company anti-diversionary rules

(Clause 10 of the Draft TLAB: Section 9D(9A) of the Income Tax Act)

- ***Comment***: The concern relating to the mere conclusion of contracts in the country of residence of the CFC is acknowledged. The proposed amendments are too restrictive to CFCs that enter into genuine business transactions with persons outside of the country of residence of the CFC. The proposed amendments should be withdrawn or alternatively the requirement for delivery should relate to the delivery of goods from the country of residence of the CFC to the South African resident rather than the delivery of goods to the CFC in its country of residence.

  ***Response*: Not Accepted.** Firstly, while Government acknowledges business practices, this loophole in the diversionary rules should be closed. Secondly, the alternative proposal suggested would still allow for the diversion of profits from South Africa, as a CFC, for example, in Country A, that signs a purchase contract with a third-party supplier in Country A, but with goods originating from another country and are delivered directly to SA. That transaction would arguably not result in imputation of net income from that transaction to South African residents.

- ***Comment***: The references in the Explanatory Memorandum of "anti-diversionary rules for CFC outbound sale of goods" in the "Reasons for change" as well as in the "Proposal" section is inappropriate.

  ***Response:* Accepted.** Changes will be made in the 2021 Draft EM to the 201 Draft TLAB to delete the references to “anti-diversionary rules for CFC outbound sale of goods”.

2021 Draft TLAB: Value Added Tax

VAT treatment of temporary letting of residential immovable property

(Clause 54 of the Draft TLAB: New section 18D of the VAT Act)

- The VAT Act makes provision for the supply of residential fixed property by a VAT vendor (being a property developer) to be subject to VAT at the standard rate of 15 per cent. This would entitle property developers to claim input tax credits. However, the leasing of residential fixed property is an exempt supply which would generally result in the input tax being denied.

- Where the property developer is unable to sell the residential fixed property and enters into a lease, until a buyer is found, the property developer is required to make an output tax adjustment based on the *open market value* of the residential fixed property when the residential fixed property is leased for the first time.

- Concerns have been raised regarding the application of the VAT provisions in this regard, especially the inequitable value attributed to this change in use adjustment.

- In order to address these concerns, it is proposed that changes be made in 2021 Draft TLAB by inserting a new section in the VAT Act that will deal with the deemed change in use adjustment when the residential fixed property is leased for the first time, including whether that deemed change in use adjustment results in the residential fixed property exiting the VAT net or not and the VAT consequences of the subsequent sale of the residential fixed property.

VAT treatment of temporary letting of residential immovable property

(Clause 54 of the Draft TLAB: New section 18D of the VAT Act)

- ***Comment:*** The change in use adjustment is in relation to fixed property that is temporarily let. The word "temporary" is linked to the intention of the vendor and as such, is subjective in nature and this is what creates the uncertainty. As such, a time limit as a proxy for intention will assist in providing certainty.

    Response: **Accepted**. The proposed amendments will be further amended to specify what is envisaged by the words "temporarily applied" by introducing a new definition in section 18D.

- ***Comment:*** The VAT payable on the change in use adjustment when the fixed immovable property is leased for the first time is still disproportionate to the exempt income earned by the developer and it is suggested that a formula be used for the adjustment which should be similar to the formula used in Australia.

    Response: **Partially Accepted**. The proposed provision is designed to ease the output tax burden faced by property developers when the fixed property is leased for the first time because the proposed provision requires the developer to make an output tax adjustment on the *adjusted cost*, not the current *open market value* of the fixed property. However, the proposed amendment will be further amended to provide clarity on the input tax and output tax adjustments.

VAT treatment of temporary letting of residential immovable property

(Clause 54 of the Draft TLAB: New section 18D of the VAT Act)

- ***Comment:*** The proposed amendments are not clear on what the situation would be where the developer chooses to permanently apply the fixed property for rental income.

  Response: **Accepted.** The proposed amendments will be further amended to clarify that in such instances the change in use will be a permanent change in use as envisaged by section 18(1), and that section 18(1) will be applicable.

- ***Comment:*** The wording in its current form creates the perception that the purchaser of the property will only be liable for the payment of VAT to the extent of the difference between the purchase price and the *adjusted cost*. In order to achieve the correct result in the circumstances, it is recommended that section 18D(4) be re-worded.

  Response: **Accepted**. The section will be re-worded to split out the input tax and the output tax adjustments. This re-wording should also clarify the situation where the vendor sells the property at a loss.

- ***Comment*:** 1st April 2022 is considered too late to assist developers who have been struggling with cash flow difficulties. The proposed amendment should be backdated to 1st January 2018 when the first relief was withdrawn or from when there was a first lockdown (26th March 2020).

  Response: **Not Accepted.** Amendments to tax legislation are usually only made retrospectively in instances of anti-avoidance measures. These proposed amendments provide relief to a specific sector of vendors (property developers registered for VAT).

2021 Draft TLAB: Carbon Tax

Clarifying renewable energy premium beneficiaries

(Clause 63 of the Draft TLAB: Section 6(2)(c) of the Carbon Tax Act)

- Section 6(2)(c) of the Carbon Tax Act makes provision for electricity generators liable for the carbon tax to offset the cost of their additional renewable energy purchases against their carbon tax liability.
- This provision was intended to address stakeholders' concerns on possible double taxation due to the introduction of the carbon tax in addition to the "renewable IPP tariff" already applied under the Renewable Energy Independent Power Producers Procurement Programme (REIPPPP).
- It has come to Government's attention that some taxpayers are of the view that the Carbon Tax Act was ambiguous on the intended beneficiaries of this concession and requested clarity on whether renewable-based self-generation with electricity wheeling arrangements through Eskom would also be eligible to claim the renewable energy premium deduction.
- To address this, the following proposed changes were included in the 2021 Draft TLAB:
  - Only entities that are liable for the carbon tax, conduct electricity generation activities and purchase additional primary renewable energy directly either under the REIPPPP or from private independent power producers would be eligible to claim the tax deduction for its renewable energy purchases, provided the power purchasing agreement/contract exists
  - It is proposed that Section 6(2)(c) of the Carbon Tax Act is amended to clarify that the Renewable energy premium to be deducted for purchases of additional renewable electricity is the product of the amount of RE purchased (kWh) under a power purchase agreement and the applicable rate for that technology as specified in the Renewable Energy Notice gazetted by the Minister of Finance, as follows: **Deduction (B) =** quantity of renewables purchased (kWh) × rate (Rand) per technology as per the Gazetted notice .

Clarifying renewable energy premium beneficiaries

(Clause 63 of the Draft TLAB: Section 6(2)(c) of the Carbon Tax Act)

- **Comment:** Although clarifications were welcomed, stakeholders were concerned that reference to allowing only renewable energy purchases made in terms of a power purchase agreement (PPA) could create uncertainty as different types of PPAs may exist. It was unclear whether a taxpayer that generates electricity from fossil fuels, has a power purchase agreement in place with a third party to purchase renewable energy and that third party supplies the electricity directly to the taxpayer for example, on-site solar PV project, and not through the national grid, would be eligible to claim the RE premium deduction. It was recommended that examples of eligible renewable energy purchases for the different PPAs are provided in the explanatory memorandum (EM).

  Response: Accepted. PPAs can exist for onsite renewable electricity purchases where there is direct supply of electricity to the buyer, and offsite electricity purchases where the producer supplies electricity to the buyer through the national grid and not directly to the buyer. Renewable electricity purchases by taxpayers in terms of an offsite PPA would be eligible however, onsite PPAs would not be eligible as it resembles self-generation for own use and would be not constitute additional electricity purchases.

  - Changes will be made in the 2021 Draft EM to the 2021 Draft TLAB to include examples of eligible renewable energy purchases under the different types of PPAs

Clarifying the definition and scope of carbon sequestration-Limitation on biological sequestration to forest plantations

(Clause 63 of the Draft TLAB: Sections 6(3) & 6(4) of the Carbon Tax Act)

- In November 2020, a methodological guideline document was published by the Department of Forestry, Fisheries and Environment (DFFE) to provide methodologies for taxpayers to use for quantifying greenhouse gas emissions sequestration in the forestry industry.
- This methodological guideline covers reporting and accounting parameters for sequestration across the forestry, paper and pulp, and manufacturing of harvested wood products (HWPs) industries.
- For forestry plantations, the DFFE provides for emissions sequestered directly by forests to be deducted from fuel combustion emissions as well emissions embedded in harvested wood products (HWPs) in line with the Intergovernmental Panel on Climate Change (IPCC) Guidelines.
- Aligning the definition of sequestration in the Carbon Tax Act with the DFFE methodological guidelines is problematic.
- Due to concerns about the permanence of sequestered emissions in HWPs and lack of control of the production processes by forestry companies beyond the mill gate and the robustness of the available emissions calculation methodologies, changes were made in the 2021 Draft TLAB that only actual forestry plantation sequestered emissions within the mill gate should be eligible for the deduction under the Carbon Tax Act. Also, changes were made to the definition of biological carbon sequestration in section 6(3)/(4) of the Carbon Tax Act to limit it only to directly sequestered emissions by forest plantations

Clarifying the definition and scope of carbon sequestration-Limitation on biological sequestration to forest plantations

(Clause 63 of the Draft TLAB: Sections 6(3) & 6(4) of the Carbon Tax Act)

- **Comment:** The industry indicates that it has engaged extensively with the Department of Forestry, Fisheries and Environment (DFFE) over several years on the development of the Draft Methodological Guidelines for Quantification of Greenhouse Gas Emissions – Carbon Sequestration in the Forestry Industry to Support the Implementation of the Greenhouse Gas Emission Reporting Regulations. It is of the view that the methodological guideline does address concerns around the permanence of sequestered emissions in harvested wood products (HWPs), the lack of control of the production processes by forestry companies beyond the mill gate and the lack of robustness of the available calculation methodologies. It is suggested that the definition and scope of the sequestration deduction in the Carbon Tax Act is aligned with the methodological guideline.

Response:Accepted. Changes will be made in the 2021 Draft TLAB to expand the scope of the sequestration deduction to also include harvested wood products for the pulp, paper and print activity. The sequestered emissions will be determined using the mass flow approach combined with the landfill approach to account for sequestered emissions as per the DFFE Carbon Sequestration Guideline, in the short term. From an emissions accounting perspective, for forestry management and HWP pools it will be important to account for gains and losses occurring from within the mill's operational boundaries. For future carbon tax periods, as recommended in the Carbon Sequestration Guidelines, the 100-year accounting approach should be developed once industry specific studies are completed on suitable half-life (product decay rates) and product use period assumptions.

Aligning schedule 2 emissions activities and thresholds with the greenhouse gas emission reporting regulations of the DFFE

(Clause 65 of the Draft TLAB: Schedule 2 of the Carbon Tax Act)

- The Carbon Tax Act came into effect on 1 of June 2019. The tax base for the carbon tax are the greenhouse gas emissions that are reported annually by taxpayers to the Department of Forestry, Fisheries and Environment (DFFE) as required under the National Greenhouse Gas Emission Reporting Regulations. Schedule 2 of the Carbon Tax Act outlines the activities that are subject to the carbon tax and is based on Annexure 1 of the National Greenhouse Gas Emission Reporting Regulations as reported emissions are subject to the carbon tax.
- On 11 September 2020 the DFFE published the amendments to the National Greenhouse Gas Emission Reporting Regulations. Annexure 1 of the GHG emissions reporting regulations was amended to include changes to the activities required to report their emissions and thresholds, and the inclusion of new activities now reportable to DFFE.
- Proposed changes were made in the 2021 draft TLAB to Schedule 2 of the carbon tax act to ensure alignment with the amended GHG Emissions reporting regulations

Aligning schedule 2 emissions activities and thresholds with the greenhouse gas emission reporting regulations of the DFFE

(Clause 65 of the Draft TLAB: Schedule 2 of the Carbon Tax Act)

- **Comment:** Stakeholders were of the view that a change that is effective from 11 September 2020 will apply to the tax period from 1 January 2020 to 31 December 2020, and result in a retrospective change in legislation. In terms of the Carbon Tax Act, the tax period is from 1 January to 31 December. This will also result in an administrative burden as the tax returns for the tax period 1 January 2020 to 31 December 2020 had already been submitted as they were due for submission on 29 July 2021. It is recommended that the amendments to Schedule 2 of the Carbon Tax Act shall apply to tax periods commencing on 1 January 2021, and aligned with the announcement in Annexure C of the 2021 Budget Review

  <u>Response: Accepted</u>. Changes will be made in the 2021 Draft TLAB to change the effective date for the Schedule 2 amendments from 11 September 2020 to 1 January 2021.

2021 Draft TALAB

2021 Draft TALAB: Income Tax

Information required in receipts issued for tax deductible donations

(Clause 2 of the draft TALAB; section 18A of the Income Tax Act)

- The information required by law in the receipts issued for tax-deductible donations is limited and entities issuing the receipts are not required to provide third-party data on the donations to SARS on a systematic basis. SARS has detected that receipts are being issued by entities that are not approved to do so. To ensure that only valid donations are claimed and to ensure that receipts and third party data provided to SARS match, it is proposed that the information required in the receipts be extended to allow such information as the Commissioner may prescribe by public notice from time to time. Third-party reporting will be extended in future to cover the receipts issued.

Comment: The proposed amendment may increase the compliance burden on public benefit organisations (PBOs), especially the smaller and unsophisticated ones that are already struggling with high compliance costs. In effect, the Commissioner may, as a result of the proposed amendment, require PBOs to file third-party returns in the future in respect of section 18A receipts issued. These smaller PBOs may not be able to comply with the third-party reporting requirements.

Response: Noted. This amendment is not required for third party reporting. The proposed amendment simply ensures consistency of the section 18A certificates with such reporting.

SARS is cognizant of the impact third party reporting may have on smaller PBOs and is therefore considering a differentiated approach, for example by providing a simpler mechanism for third party reporting by smaller PBOs.

Information required in receipts issued for tax deductible donations (cont.)

(Clause 2 of the draft TALAB; section 18A of the Income Tax Act)

The aim of third party reporting is to make it easier for those receiving the receipts (donors), as well as those issuing the receipts (PBOs), to comply with their obligations. SARS will be able to auto populate returns thereby making it easier for donors to claim their valid donations. It will encourage donations to PBOs by donors and lessen the burden on PBOs where taxpayers approach them for additional documentation requested by SARS during the verification process. PBOs will also be protected from fraudulent claims using their details and the reputational impact such claims have.

Administrative non-compliance penalties for non-submission of six-monthly employees' tax (EMP501) returns

(Clause 6 of the Draft TALAB: Paragraph 14(6) of Fourth Schedule to Income Tax Act)

- SARS may impose a penalty for the non-submission of the six-monthly employees' tax returns by employers. The penalty is calculated as a percentage of the employees' tax for the period covered by the return. Where the employees' tax for the period is not known to SARS, due to the non-submission of monthly or six-monthly returns, the penalty can only be imposed retrospectively. This undermines the purpose and deterrent effect of the non-compliance penalty. The proposed amendment enables SARS to raise the penalty on an alternative basis in such cases, through an estimate of the employees' tax using data readily available to SARS with an adjustment once the actual employees' tax is known.

Comment: While it is clear that the purpose of levying penalties is to act as a deterrent against non-compliance, it is proposed that further clarity be provided on how the estimation will be calculated.

Response: Noted. The PAYE administrative non-compliance penalty will be estimated using data readily available to SARS; for example, prior monthly or six-monthly liability details where such liability is not available for the reconciliation period that is outstanding. In addition, SARS may use information relating to salary paid per the corporate income tax return in order to estimate the PAYE liability on which to base the PAYE administrative penalty calculation.

Administrative non-compliance penalties for non-submission of six-monthly employees' tax (EMP501) returns (cont.)

(Clause 6 of the Draft TALAB: Paragraph 14(6) of Fourth Schedule to Income Tax Act)

Comment: Where the employees' tax is overestimated, this will result in a higher interim penalty being levied. Upon correction at a later stage, an adjustment to a lower penalty amount may increase the unallocated payments against the taxpayer's SARS account.

> ***Response:*** Noted. Account and payment processing needs will be monitored. The current legislation permits SARS to adjust the penalty in line with changes in the liability of the taxpayer and this principle applies to personal and corporate income tax administrative penalties as well.

Comment: It appears that an EMP501 submitted via e@syfile is regarded as not being submitted on eFiling if SARS performs an Employment Taxes Verification (ETV) on the return. It is submitted than an EMP501 should not be regarded as not being submitted if it is subject to the SARS ETV process. The EMP501 should be reflected on the SARS system as being submitted but it should then be flagged as being under review, to prevent the proposed non-submission penalty from being raised incorrectly.

> ***Response:*** Accepted. e@syFile and eFiling submissions are treated in the same manner and all submissions may go through the ETV process. When the reconciliation is submitted, the status is updated to received, regardless of the ETV process being initiated or not. This matter has been further discussed with the commentator, which undertook to raise it through the recognised controlling body (RCB) channels for SARS to investigate should it resurface with the RCB member who raised it or more broadly.

Removal of double penalty

(Clause 9 of the Draft TALAB: Paragraph 17 of Seventh Schedule to Income Tax Act)

- Under paragraph 13 of the Fourth Schedule to the Income Tax Act, employers have an obligation to issue Employees' Tax Certificates (IRP5/IT3(a) certificates) to their employees. The Employees' Tax Certificate must reflect the total remuneration including the amount of any fringe benefit and allowance, and the sum of employees' tax (PAYE) deducted during that period. If the employer under deducts PAYE and under pays SARS as a result of understating taxable fringe benefits SARS must impose a penalty of 10% on the underpayment.

- The employer has an obligation to determine the cash equivalent of the value of the taxable benefit granted to its employees. Paragraph 17 of the Seventh Schedule to the Income Tax Act provides that the nature of the taxable benefit and the cash equivalent of the value thereof must be reflected on the Employees' Tax Certificate or a separate certificate. If an employer fails to comply with this requirement, SARS may impose a penalty equal to 10% of the amount by which the cash equivalent is understated.

- Two separate penalties may thus be imposed for the same understatement. The proposed amendment removes this double penalty.

Removal of double penalty (cont.)

(Clause 9 of the Draft TALAB: Paragraph 17 of Seventh Schedule to Income Tax Act)

Comment: Whilst we expect the proposed amendment would be welcomed by most tax practitioners and taxpayers, consideration should be given to whether the paragraph 17 penalty should remain. Additional safeguards must be in place to ensure accurate determination of fringe benefits – hence the paragraph 17 penalty. At the same time, however, taxpayers should not be penalised under the Fourth and the Seventh Schedules where the mistake is the understatement of PAYE merely because of the understatement of fringe benefits. It is therefore proposed that the Seventh Schedule penalty should only apply where an employer has understated the value of fringe benefits on the IRP5 but not for the purpose of completion of the EMP201.

Response: Not accepted. The PAYE penalties are wide-ranging, and it is submitted will always be imposable in situations where the fringe benefit was not declared on the certificate to the detriment of the *fiscus*.

2021 Draft TALAB: Customs and Excise

Interpretation of expression "Trade and Industry" where it occurs in certain provisions of the Customs and Excise Act

(Clause 10 of the Draft TALAB: Sections 4, 21A, 43, 48, 53, 55, 56, 56A, 75 and 114 of the Act)

- The proposed amendment aims to correct the different references in the Customs and Excise Act to the Department currently known as the Department of Trade, Industry and Competition.

Comment: The proposed provision is drafted in such a way that it doesn't actually amend the expressions in the Customs and Excise Act, but merely requires them to be read in a certain way. This would result in the Customs and Excise Act always having to be read with the TALAA, 2021. The changes should be made by way of amendments to the Customs and Excise Act.

Response: Partially accepted. Rather than amend multiple provisions in the Customs and Excise Act relating to the name change, clause 10 will be replaced by an amendment of section 1 of the Customs and Excise Act providing for the insertion of the interpretation provision as a new subsection (5A).

Deletion of reference to accreditation for purposes of changes in SARS' accreditation system

(Clause 12 of the Draft TALAB: Section 38A of the Customs and Excise Act)

- The effect of the proposed amendment is that not only accredited licensees or exporters will be able to supply goods to foreign going ships or aircrafts on the issuing by that such licensee or exporter of a dispatch and delivery note or such other document as the Commissioner may prescribe or approve by rule. This amendment is proposed as a result of the announcement in Budget 2021 that SARS is changing its accreditation system to more closely reflect the requirements of the SAFE Framework of Standards issued by the World Customs Organisation. The effect of the new accreditation system is that certain provisions in the Act requiring a person to have accredited client status were reviewed.

Comment: A simultaneous amendment to section 21(3)*(c)* of the Customs and Excise Act, is proposed so as to ensure uniformity with the announcement that was contained in the Budget Review, 2021.

Response: **Not accepted.** Rules under section 64E containing detail with respect to the new SARS accreditation system were promulgated on 23 July 2021. The effect of the new accreditation system is that certain provisions in the Act requiring a person to have accredited client status were reviewed, for example section 38A(2)*(a)*(i). Section 21(3)*(c),* providing that only importers who are accredited may store imported goods which are free of duty in special customs and excise storage warehouses for export, is retained. The reason being that the payment of VAT on these goods is deferred while the goods are stored in a special customs and excise storage warehouse. This is still considered a benefit that only accredited importers should have.

Increasing the minimum thresholds for underpayments of duty by taxpayers and of refunds by SARS to ease administrative burden

(Clauses 13 and 16 of the Draft TALAB: Sections 47(1) and 76(5) of the Customs and Excise Act)

- The proposed amendments to section 47(1) aims to ease the administrative burden on taxpayers and on SARS by increasing the minimum thresholds for underpayments of duties by taxpayers, which the Commissioner may condone. A similar amendment is proposed in respect of section 76(5) in relation to minimum thresholds for refunds of duty to taxpayers.

Comment: A consequential amendment is proposed to the Value-Added Tax Act, 1991, to ensure alignment of the minimum values as it relates to VAT levied upon importations as well as VAT amounts paid upon importation on which refunds are claimed.

Response: Partially accepted. The suggestion deserves further consideration but the interaction between VAT and duty raises difficult questions in this context. As a result, this amendment is withdrawn for further consideration of the potential for an integrated approach.

Extension of period within which taxpayer can request revision of an assessment based on an estimate

(Clause 18 of the Draft TALAB: Section 95 of the Tax Administration Act)

- SARS may make an original, additional, reduced or jeopardy assessment based in whole or in part on an estimate, if the taxpayer does not submit a response to a request for relevant material after delivery of more than one request for such material. The taxpayer may, within 40 business days from the assessment, request SARS to issue a reduced or additional assessment by submitting the relevant material. A senior SARS official may extend the 40 business day period for a period not exceeding the relevant prescription periods under section 99 of the Act.

- It may happen that SARS issues an additional estimated assessment close to the end of the relevant prescription period. The 40 business day period may thus end after the prescription date or very close to it, which means that the taxpayer is unable to request a reduced or additional assessment. The proposed amendment aims to address these unusual circumstances.

Extension of period within which taxpayer can request revision of an assessment based on an estimate (cont.)

(Clause 18 of the Draft TALAB: Section 95 of the Tax Administration Act)

Comment: In order to achieve and clarify what the amendment sets out to do, i.e. to provide SARS with the opportunity to extend the period in which a taxpayer may request a revision of an estimated assessment for up to forty days after the prescription date, the following wording is proposed:

"(7) A senior SARS official may extend the period referred to in subsection (6) within which the return or relevant material must be submitted, for a period not exceeding forty business days after the relevant period referred to in section 99(1)."

Response: Not accepted. The proposed wording does not take account of the fact that the end of the initial period to request a reduced or additional assessment may fall after the prescription date, so the forty-day extension may fall later than forty days after the date. It also provides for an extension past prescription, even where prescription is not an issue due to the timing of the making of an assessment based on an estimate. The current wording of the proposed amendment is regarded as clear as to the purpose it seeks to achieve.

Extension of period within which taxpayer can request revision of an assessment based on an estimate (cont.)

(Clause 18 of the Draft TALAB: Section 95 of the Tax Administration Act)

Comment: To the extent that the taxpayer has submitted the relevant information before the prescription date, the Commissioner is mandated to revise the assessments to reflect the correct outcome. It now appears that the taxpayer's submission of the relevant information to the Commissioner before the expiry of timelines does not guarantee the issuing of the revised assessments, as such a decision will depend on the Commissioner's discretion.

Response: Noted. Based on the proposed revised wording of section 95(5) and (6), once a taxpayer submits the relevant material as required in terms of section 95(6), SARS has one of the following three options and the taxpayer may respond accordingly:

- Option 1: After review SARS accepts the relevant material and makes a reduced or additional assessment as requested by the taxpayer
- Option 2: After review SARS does not accept some of the relevant material and makes a reduced or additional assessment accordingly. In this instance, the reduced or additional assessment will be subject to objection and appeal in the ordinary course, since it replaces the assessment contemplated in section 95(1)*(a)* or *(c)*
- Option 3: After review SARS does not accept any of the relevant material, does not make a reduced or additional assessment and relies on the assessment based on an estimate. In this regard the proposed new section 95(8) clarifies that, should SARS decide not to make a reduced or additional assessment, the taxpayer may object and appeal within the normal timeframes from the date of the decision.

Extension of period within which taxpayer can request revision of an assessment based on an estimate (cont.)

(Clause 18 of the Draft TALAB: Section 95 of the Tax Administration Act)

Comment: The proposal that the Commissioner may extend prescription or not in terms of his/her discretion may have adverse consequences against the taxpayer. It is requested that some certainty is required in terms of how the Commissioner's discretion will be exercised or alternatively, the relevant factors that the Commissioner will consider when exercising his/her discretion.

Response: Partially accepted. SARS' discretion in granting the extension requested under section 95(7) is governed by section 33 of the Constitution, 1996, read with Promotion of Administrative Justice Act, 2000, (PAJA) which gives effect to section 33. It is required to be lawful, reasonable and procedurally fair as required by the circumstances of each case. As such circumstances will differ from case to case, it is not possible to legislate the criteria for all foreseeable circumstances that can lead to a request for an extension. However, it is proposed to align the wording with the approach taken in the Tax Administration Act in respect of certain other extension decisions, namely that SARS may extend the period if reasonable grounds for an extension are submitted by the taxpayer.

Extension of period within which taxpayer can request revision of an assessment based on an estimate (cont.)

(Clause 18 of the Draft TALAB: Section 95 of the Tax Administration Act)

Comment: Section 95 should include some wording that requires the Commissioner to request the relevant information within a reasonable timeframe, such as the proposed 40-day period before prescription to afford the taxpayer sufficient time to adequately address the request from the Commissioner. Affording the Commissioner the opportunity to raise assessments first "without the reasonable timeframe requirement for the Commissioner to request information" may disadvantage the taxpayer.

> ***Response:*** Not accepted. Where SARS raised an assessment based on an estimate under section 95(1)*(c)*, it would be in instances where SARS requested relevant material from the taxpayer on more than one occasion, without receiving a response to those requests. Section 95(6), read together with section 95(7), then provides the taxpayer with up to 80 business days to submit the relevant material even when prescription is an issue. This is regarded as sufficient time in order for the taxpayer to comply with the requirements of section 95(6).

Comment: Clarity is sought as to the form of the notice that SARS will issue to a taxpayer in the event of a taxpayer submitting relevant material in terms of section 95(6), where SARS finds that the material does not support an adjustment to the estimated assessment.

> ***Response:*** Noted. In the event that SARS finds that the return or relevant material submitted does not support the making of a reduced or additional assessment, a letter will be issued to the taxpayer, containing SARS' grounds for the decision.

Extension of prescription in certain instances

(Clause 19 of the Draft TALAB: Section 99 of the Tax Administration Act)

- The proposed amendment is consequential to the amendments to section 95 of the Tax Administration Act, and provides that the prescription periods not apply to the extent that the period for providing relevant material under section 95(6) falls after the normal prescription periods.

Comment: While it is acknowledged that prescriptions would have to be extended in the circumstances envisaged by section 95(7), the proposed amendment seemingly results in prescription never applying to the tax period in question. The extension of prescription should be only for a limited period and not in perpetuity.

> ***Response:*** Comment misplaced. Where a taxpayer submits a request in terms of section 95(7) for an extension of the initial 40-business day period, such extension is limited to a maximum of 40 business days post the initial 40-business day period under section 95(6) and prescription would not apply to the extent that this period exceeds the relevant prescription periods contained in section 99(1). That is to say for a maximum of 80 business days. In the light of the following comment, however, the proposed amendment to section 99(2)*(e)* will be replaced by a proposed amendment to section 99(2)*(d)*(iv) to provide that prescription will not apply to the extent that it is necessary to give effect to a reduced or additional assessment requested under section 95(6).

Extension of prescription in certain instances (cont.)

(Clause 19 of the Draft TALAB: Section 99 of the Tax Administration Act)

<u>Comment:</u> The current proposal only allows SARS to reduce an assessment post prescription if the period within which the request should have been was extended post prescription in line with the proposal in clause 18 of the draft Bill. It is proposed that section 99 be further amended to allow SARS to issue a reduced assessment post prescription where the section 93(1)*(f)* reduced assessment request was made prior to prescription, similar to section 99(2)*(d)*(iii) in respect of section 93(1)*(d)* reduced assessment requests. In our view, this is required especially absent any time period within which SARS must issue reduced assessments under section 93(1)*(f)* (we will submit this matter as part of the Annexure C proposals).

> ***<u>Response:</u>*** <u>Accepted.</u> The amendment to section 95 to include the proposed new subsection (7), read with the amendment to section 99(2)*(d)* to include the proposed new item (iv), allows SARS to issue a reduced assessment post prescription where the reduced assessment request was made within the prescribed period.

2021 Draft TALAB: Disaster Management Tax Relief Administration

Expansion of deferral of payment of employees' tax liabilities for tax compliant small to medium sized businesses

(Clause 1 Second Batch: Section 1 of the Disaster Management Tax Relief Administration Act)

Despite the relaxation of the national lockdown, various businesses and employees are still negatively impacted by the COVID-19 pandemic. These negative impacts are further exacerbated by the impacts of the recent unrest in the country that destroyed businesses and infrastructure. The Government, therefore, wishes to provide additional assistance to those who continue to be adversely affected by COVID-19 as well as assisting in the process of reconstructing businesses.

As a result, it is proposed that the PAYE deferral relief measure be reinstated for another limited three-month period as follows:

- Deferral of payment of 35 per cent of the PAYE liability, without SARS imposing administrative penalties and interest for the late payment thereof
- The deferred PAYE liability for the three-month period of August to October 2021 must be paid to SARS in equal instalments over a four-month period commencing on 1 November 2021, (i.e. the first payment must be made on 7 December 2021)
- The proposal will be available to small or medium sized businesses conducted by a company, partnership, individual or trust with a gross income not exceeding R100 million for the year of assessment ending on or after 1 April 2021 but before 1 April 2022

Expansion of deferral of payment of employees' tax liabilities for tax compliant small to medium sized businesses (cont.)

(Clause 1 Second Batch: Section 1 of the Disaster Management Tax Relief Administration Act)

- The inclusion of a limitation that gross income should not include more than 20 per cent of income derived from interest, dividends, foreign dividends, royalties, rental from letting fixed property, annuities and any remuneration received from an employer
- Rental income derived from the letting of fixed property excludes rental income derived by a person whose primary trading activity is the letting of fixed property and substantially the whole of the gross income is rental from fixed property
- The requirement that the employer is tax compliant in terms of the Tax Administration Act when making a reduced payment
- To qualify for this relief measure, the employer will need to have been registered with SARS as an employer by 25 June 2021.

The proposed measures will come into operation on 1 August 2021 and end on 31 October 2021.

Expansion of deferral of payment of employees' tax liabilities for tax compliant small to medium sized businesses (cont.)

(Clause 1 Second Batch: Section 1 of the Disaster Management Tax Relief Administration Act)

Comment: To qualify for the new PAYE and Employment Tax Incentive (ETI) relief, a taxpayer must be a 'qualifying taxpayer' which is defined as a person conducting a trade. Public Benefit Organisations (PBOs) approved in terms of section 30 of the Income Tax Act and many other exempt organisations such as recreational clubs, professional bodies and schools are effectively excluded from this definition as most of them do not conduct a trade.

As these organisations, especially PBOs, play a significant role in our society and have been affected dramatically by the COVID-19 lockdown (and will be affected for many months thereafter as they may no longer receive donations that they previously relied upon), we submit that the definition of 'qualifying taxpayer' should be amended to include these organisations as mentioned above.

> ***Response:*** Not accepted. The design of these measures mirrors that of the measures in 2020 in order to enable their speedy implementation without significant systems development on the part of employers, payroll providers and SARS. As noted when a similar comment was made with respect to the Disaster Management Tax Relief Administration Bill, 2020, automatic PAYE relief is targeted at small to medium sized businesses. Gross income, which is a key requirement, is a poor measure of PBOs' size, since their receipts are often of a capital nature. PBOs may apply for case-by-case relief by SARS, where their actual circumstances can be properly considered. The concept of a qualifying taxpayer is not used in the ETI relief measure.

THANK YOU