# RESPONSE ON THE 2021 TAX BILLS

Presentation to the Select Committee on Finance (SECoF)

PRESENTED BY:

*National Treasury & SARS*

**Date: 8 December 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.
- National Treasury and SARS received written comments from 76 contributors on the 2021 Draft Tax Bills by deadline of 28 August 2021.

# CONSULTATION PROCESS

- 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 presented to the SCoF a draft response document containing a summary of draft responses to public comments received on the 2021 Tax Bills.
- 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.
- The 2021 Tax Bills were introduced by the Minister in the National Assembly on 11 November 2021.
- The SCoF voted on the 2021 tax bills on 24 November 2021.
- On 30 November 2021, National Treasury and SARS briefed the SECoF on the key issues on the 2021 Tax Bills.
- On 7 December 2021, SECoF held public hearings on the 2021 Tax Bills
- Today, 8 December 2021, National Treasury and SARS present to the SECoF a response on the key issues raised during public hearings on the 2021 Tax Bills.

# 2021 Rates Bill: Increase in excise duties on tobacco

# General increase in the excise duty on 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*:** What is proposed in the Draft Rates Bill – an 8% excise increase on cigarettes – is unjustifiable in the context of a projected inflation rate of only 4.9%.

> ***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 hike proposed in the Bill will put the excise incidence on the cigarette's Most Popular Price Category (MPPC) at 45%, which is 12.5% or 5 percentage points higher than what National Treasury's own excise policy stipulates.

> ***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 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.

# Illicit trade of 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.

# THANK YOU